

No. 15755

United States
Court of Appeals
for the Ninth Circuit

MERRIMAN H. HOLTZ and HELEN TYROLL
HOLTZ,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,
Respondent.

Transcript of Record

Petition to Review a Decision of the Tax Court
of the United States

FILED

DEC 11 1957

PAUL P. O'BRIEN, CLERK

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[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

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APPEARANCES

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Portland, Oregon,
For the Petitioners.

CHARLES K. RICE,
Asst. U. S. Atty. Gen.;

LEE A. JACKSON,
Atty., Dept. of Justice,
Washington 25, D. C.,
For the Respondent.

The Tax Court of the United States

Docket No. 58455

MERRIMAN H. HOLTZ and HELENE TYROLL
HOLTZ,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DOCKET ENTRIES

1955

June 13—Petition received and filed. Petitioner notified. Fee paid.

June 14—Copy of petition served on General Counsel.

July 28—Answer filed by General Counsel.

July 28—Request for hearing in Portland, Oregon, filed by General Counsel.

Aug. 3—Notice issued placing proceeding on Portland, Oregon, calendar. Service of Answer and Request made.

1956

Feb. 17—Hearing set April 30, 1956, Portland, Oregon.

Apr. 13—Motion to continue to the next Portland, Oregon, calendar, filed by Petitioner. Granted April 16, 1956. Served April 17, 1956.

Nov. 26—Hearing set Feb. 18, 1957, Portland, Oregon.

1957

- Feb. 4—Hearing set Feb. 19, 1957, Portland, Oregon. Revised as to trial date.
- Feb. 19—Hearing had before Judge Withey on the merits. Submitted. Stipulation of Facts filed. Briefs due April 22, 1957. Reply Briefs due May 22, 1957.
- Apr. 8—Transcript of Hearing, 2/19/57, filed.
- Apr. 18—Motion for extension of time to May 6, 1957, to file brief, filed by Respondent. Granted 4/22/57. Served 4/25/57.
- Apr. 29—Brief filed by Petitioner. Served 5/7/57.
- May 6—Brief filed by Respondent. Served 5/7/57.
- June 6—Reply Brief filed by petitioner. Served 6/7/57.
- June 26—Memorandum Opinion rendered, Judge Withey. Decision will be entered for the respondent. Served 6/26/57.
- June 26—Decision entered, Judge Withey, Div. 4. Served 6/27/57.
- Sept. 17—Petition for Review by U. S. Court of Appeals for the Ninth Circuit, filed by petitioner.
- Sept. 17—Statement of Points, filed.
- Sept. 17—Designation of Contents of Record on Review, filed.
- Sept. 18—Proof of service of petition for review, Statement of Points and Designation of Contents of Record, filed.

The Tax Court of the United States

Docket No. 58455

MERRIMAN H. HOLTZ and HELENE TYROLL
HOLTZ,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION

The above-named petitioners hereby petition for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency (Bureau Symbols Ap:P:AA:REK 90D:LS), dated March 14, 1955, and as a basis of their proceeding allege as follows:

1. The petitioners are husband and wife, with residence at Portland, Oregon. The returns for the period here involved were filed with the Collector of Internal Revenue at Portland, Oregon.

2. The notice of deficiency (a copy of which is attached and marked Exhibit A) was mailed to the petitioners on March 14, 1955.

3. The deficiency as determined by the Commissioner is in income taxes for the calendar years and in the amounts as follows:

Year	Income Tax Liability	Assessed	Deficiency
1949	\$ 958.30	—0—	\$ 958.30
1950	671.66	—0—	671.66
Totals	\$1,629.96	—0—	\$1,629.96

The entire amount of tax deficiency is in dispute.

4. The determination of tax set forth in the said notice of deficiency is based on the following errors:

(a) The Commissioner erred in his determination that the deduction of \$83,316.29 claimed as a business bad debt in the return filed by the petitioners for the year 1950, represented a non-business bad debt under Section 23(k)(4) of the Internal Revenue Code of 1939, limited as a deduction to the extent provided in Sections 117(d)(2) and 117(e)(1) of the Internal Revenue Code of 1939.

(b) The Commissioner erred in his alternative contention that the deduction of \$83,316.29 claimed as a business bad debt was a loss not resulting in a net operating loss under the limitations prescribed by Section 122(d)(5) of the Internal Revenue Code of 1939.

5. The facts upon which the petitioners rely as a basis of this proceeding, are as follows:

The petitioner, Merriman H. Holtz, has for many years been engaged in organizing, financing, managing and participating in the operation of several corporations and businesses. The principal business of these corporations and businesses consisted of distribution, sale and rental of motion picture films and accessories, and related businesses.

The corporations were the Screen Adette Equipment Corporation, Screen Adettes Inc., and Pic-

tures Inc., all of which were organized under charters granted by the State of Oregon, and Audio Film Center was operated by the petitioner as an individual. The petitioner was also the principal stockholder and President of Helene's Inc., an Oregon corporation, operating a ladies apparel retail store in the City of Portland, Oregon. In addition to his activities in connection with these various corporations, during 1949 and 1950, as well as before and after those particular years, the petitioner engaged in the sale and rental of films and audio visual equipment operating as an individual. All of these activities, as above related, occupied his full time during the years 1949 and 1950.

The Commissioner in his deficiency has treated as a non-business bad debt the sum of \$83,316.29, which was deducted on petitioners' 1950 return. This deduction represents payments made in January and March, 1950, by the petitioners as guarantors to the United States National Bank of Portland, Oregon, on notes of the Screen Adette Equipment Corporation. This corporation was organized in 1945 to engage in the sale and distribution of motion picture equipment and accessories, with offices in Seattle, Washington; Portland, Oregon; San Francisco and Los Angeles, California. The petitioners were the owners of 500 of 503 shares of its outstanding capital stock, and was its President and General Manager. The loans made to this corporation by the United States National Bank were essential for the expansion required in con-

nection with its normal growth. The petitioners personally guaranteed these corporate loans and pledged as collateral for their guarantee, shares of common stocks then owned by them individually. In October, 1949, the corporation filed a voluntary petition in bankruptcy in the United States District Court for the District of Oregon, and said corporation never resumed any active business operation, and was dissolved by proclamation of the Governor of the State of Oregon on December 29, 1950. In the administration of the bankruptcy proceeding, creditors did not receive payment in full of their debts, and in fact received only .038 per cent upon such amounts as were due to them.

During the years 1949 and 1950, the petitioner was also President of Pictures Inc., an Oregon corporation, which was inactive since its incorporation in 1930, but which began its operations in the year 1949, and in which year petitioner advanced funds to this corporation as were required for working capital. The petitioners (husband and wife) owned 99 of the 100 outstanding shares of the capital stock of this corporation. During the years 1949 and 1950, the petitioners (husband and wife) owned 91 of the 100 outstanding shares of capital stock of Screen Adettes, Inc., an Oregon corporation. This corporation had been active for a number of years since its organization in 1932, and the petitioners made advances from time to time to the corporation for working capital. In October, 1949, a loan of \$1,000.00 was made, and this was

repaid in monthly installments in 1951. Merriman H. Holtz, one of the petitioners, was the President and managing officer of this corporation.

During the years 1949 and 1950, petitioners (husband and wife) were also the owners of 90 per cent of the outstanding capital stock of Helene's Inc., an Oregon corporation. For a considerable number of years, at least as far back as 1943, this corporation had borrowed funds from the bank for working capital. The amount of the loans outstanding during these periods varied from approximately \$10,000.00 to \$25,000.00. All of these bank loans were guaranteed by the petitioners, who had pledged as collateral to secure their guarantees, shares of common stocks owned by them, as well as life insurance policies carried on the lives of the petitioners. The corporation suffered increasingly substantial losses in its business after moving to a new location in 1947, and in 1949 all of its assets were sold and the corporation's creditors were paid approximately 50 per cent in full settlement of their debts. The final return of the corporation was filed for its fiscal year ending January 31, 1950.

Wherefore, the petitioners pray that this Court may hear the proceeding and determine:

(a) That the petitioners are not liable for additional income tax for the years 1949 and 1950, and that the petitioner's returns filed for 1949 and 1950 are proper and valid as filed.

(b) That the payment of \$83,316.29 to The United States National Bank of Portland by petitioners in January and March, 1950, entitles them to deduct said amount as a business bad debt resulting in a net operating loss and not limited under Section 122(d)(5) of the Internal Revenue Code of 1939.

/s/ MERRIMAN H. HOLTZ,

/s/ HELENE TYROLL HOLTZ,
Petitioners.

/s/ MOE M. TONKON,
Attorney for Petitioners.

Duly verified.

EXHIBIT A

Form 1230 (App.)

U. S. Treasury Department
Internal Revenue Service
Regional Commissioner
Appellate Division
P. O. Box 3935
Portland 8, Oregon

In Replying Refer to
Ap:P:AA:REK
90D:LS

Merriman H. and Helene Tyroll Holtz,
3707 S. W. Chehalem Street,
Portland, Oregon,

Dear Mr. and Mrs. Holtz:

You are advised that the determination of your income tax liability for the taxable year(s) ended December 31, 1949 and December 31, 1950 discloses a deficiency or deficiencies of \$1,629.96 as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency or deficiencies mentioned.

Within 90 days from the date of the mailing of this letter you may file a petition with The Tax Court of the United States, at its principal address, Washington 4, D. C., for a redetermination of the deficiency. In counting the 90 days you may not exclude any day unless the 90th day is a Saturday, Sunday, or legal holiday in the District of Columbia in which event that day is not counted as the 90th day. Otherwise Saturdays, Sundays, and legal holidays are to be counted in computing the 90-day period.

Should you not desire to file a petition, you are requested to execute the enclosed form and forward it to the Assistant Regional Commissioner, Appellate, P. O. Box 3935, Portland 8, Oregon. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency or deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after receipt of the form, or on the date of assessment, or on the date of payment, whichever is the earlier.

Very truly yours,

T. COLEMAN ANDREWS,
Commissioner,
Internal Revenue Service.

By /s/ A. N. WILLIAMS,
Associate Chief,
Appellate Division.

Enclosures:

Statement
Form 1276
Agreement Form

Statement

Ap:P:AA:REK

90D:LS

Merriman H. and Helene Tyroll Holtz
3707 S. W. Chehalem Street
Portland, Oregon

Tax liability for the taxable years ended December 31, 1949,
and December 31, 1950:

Income Tax

Year	Liability	Assessed	Deficiency
1949	\$ 958.30	—0—	\$ 958.30
1950	671.66	—0—	671.66
	<hr/>	<hr/>	<hr/>
Totals	\$1,629.96	—0—	\$1,629.96
	<hr/> <hr/>	<hr/> <hr/>	<hr/> <hr/>

In making this determination of your income tax liability, careful consideration has been given to the report of examination transmitted September 17, 1952.

A copy of this letter and statement has been mailed to your representative, Mr. Moe M. Tonkon, Attorney, Public Service

Building, Portland 4, Oregon, in accordance with the authority contained in the power of attorney executed by you.

Taxable Year Ended December 31, 1949
Adjustments to Net Income

Net income as disclosed by return	\$7,920.19
Net income adjusted	\$7,920.19

Explanation of Adjustments

See Explanation of Adjustments for taxable year ended December 31, 1950.

Computation of Tax

Net income adjusted	\$7,920.19
Less: Exemptions	2,400.00
Balance subject to tax	\$5,520.19
One-half of \$5,520.19—joint return	\$2,760.10
Tentative tax on \$2,760.10	\$ 567.22
Less tax reduction: 17% of \$400.00	\$ 68.00
12% of \$167.22	20.07
Balance	\$ 479.15
Total tax liability—2 times \$479.15.....	\$ 958.30

Assessed:

Liability disclosed by return—original account No. 7606925—Oregon.....	\$958.30
Overassessment, allowance of tentative carry-back adjustment—9/12/51	
Schedule No. IT:CB:32637	(958.30)
Deficiency	\$ 958.30

Taxable Year Ended December 31, 1950

Adjustments to Net Income

Net income (loss) as disclosed by return	(\$76,656.23)
Unallowable deductions and additional income:	
(a) Bad debts disallowed	83,316.29
Total	<u>\$ 6,660.06</u>
Nontaxable income and additional deductions:	
(b) Capital loss allowed	1,000.00
Net income adjusted	<u><u>\$ 5,660.06</u></u>

Explanation of Items

(a) Bad debts disallowed:

It is determined that there is no net operating loss to be carried back to the year 1949 as explained below, and that there is a deficiency in tax of \$958.30 for that year due to the allowance of a tentative carry-back adjustment made under date of September 12, 1951.

It is determined that the deduction of \$83,316.29 claimed as a business bad debt in your return for the year 1950 represented a nonbusiness bad debt under Section 23(k)(4) of the Internal Revenue Code of 1939 limited as a deduction to the extent provided in Sections 117(d)(2) and 117(e)(1) of the Internal Revenue Code of 1939.

In the alternative it is held that the deduction represented a loss in a transaction entered into for profit under Section 23(e)(2) of the Internal Revenue Code of 1939 and that such loss does not result in a net operating loss under the limitations prescribed by Section 122(d)(5), Internal Revenue Code of 1939.

(b) Capital loss allowed:

Since the 1950 return reflects a net operating loss, no capital loss was deducted in accordance with the provisions of Section 122(d)(4), 1939 Internal Revenue Code. Adjustment (a), above, eliminates any 1950 net operating loss, and the maximum capital loss deduction of \$1,000.00 is allowed under the provisions of Section 117(d)(2), 1939 Internal Revenue Code. As shown by the return, capital loss carry-overs to 1950 exceeded 1950 capital gain by more than \$1,000.00.

Computation of Tax

Net income adjusted	\$5,660.06
Less: Exemptions	1,800.00
Balance subject to tax	<u>\$3,860.06</u>
One-half of \$3,860.06—joint return	<u>\$1,930.03</u>
Tentative tax on \$1,930.03	\$ 386.01
Less tax reduction—13% of \$386.01	50.18
Balance	<u>\$ 335.83</u>
Total tax liability—2 times \$335.83	<u>\$ 671.66</u>
Assessed:	
Liability disclosed by return—original account No. 7511064—Oregon	<u>—0—</u>
Deficiency	<u><u>\$ 671.66</u></u>

Received and filed June 13, 1955, T.C.U.S.

Served June 14, 1955.

[Title of Tax Court and Cause.]

ANSWER

Comes Now the Commissioner of Internal Revenue, by his attorney, John Potts Barnes, Chief Counsel, Internal Revenue Service, and for answer to the petition filed herein, admits and denies as follows:

1. Admits the allegations of paragraph 1 of the petition.
2. Admits the allegations of paragraph 2 of the petition.

3. Admits the allegations of paragraph 3 of the petition.

4. Denies the allegations of paragraph 4 of the petition.

5. Admits that the corporations were the Screen Adette Equipment Corporation, Screen Adettes Inc., and Pictures Inc., all of which were organized under charters granted by the State of Oregon, and Audio Film Center was operated by the petitioner as an individual. Admits that the petitioner was also the principal stockholder and president of Helene's Inc., an Oregon corporation, operating a ladies' apparel retail store. Admits that the Commissioner in his deficiency has treated as a non-business bad debt the sum of \$83,316.29 which was deducted on petitioners' 1950 return. Admits that Screen Adette Equipment Corporation was organized in 1945 to engage in the sale and distribution of motion picture equipment and accessories, with offices in Seattle, Portland, San Francisco, and Los Angeles. Admits that the petitioners were the owners of 500 of 503 shares of its outstanding capital stock and were its president and general manager. Admits that in October, 1949 the Screen Adette Equipment Corporation filed a voluntary petition in bankruptcy in the United States District Court for the District of Oregon, and was dissolved by proclamation of the Governor of the State of Oregon on December 29, 1950. Admits that during the years 1949 and 1950 the petitioner was also president of Pictures Inc., an Oregon corpora-

tion, which was inactive since its incorporation in 1930, but which began its operations in the year 1949. Admits that the petitioners owned 99 of the 100 outstanding shares of the capital stock of Pictures Inc. Admits that during the years 1949 and 1950 the petitioners owned 91 of the 100 outstanding shares of the capital stock of Screen Adettes Inc., an Oregon corporation, and that this corporation had been active for a number of years since its organization in 1932. Admits that the petitioner, Merriman H. Holtz was the president and managing officer of Screen Adettes Inc. Admits that during the years 1949 and 1950 the petitioners were also the owners of 90 per cent of the outstanding stock of Helene's Inc., an Oregon corporation. Denies the remaining allegations of paragraph 5 of the petition.

6. Denies generally each and every allegation of the petition not hereinabove specifically admitted, qualified, or denied.

Wherefore, it is prayed that the relief sought in the petition be denied and that the deficiencies in income tax, as set forth in the notice of deficiency, be in all respects approved.

/s/ JOHN POTTS BARNES,
Chief Counsel.

Filed July 28, 1955, T.C.U.S.

[Title of Tax Court and Cause.]

STIPULATION OF FACTS

It is hereby stipulated by and between the parties hereto, appearing by and through their respective attorneys of record, that the following facts are true, and that the same may be so considered and accepted by the Court as offered in evidence by the parties at the trial in the above entitled case:

1. The petitioners are husband and wife, and have had their residence in Portland, Oregon since prior to 1930, except for the years 1943 to 1945 when Merriman H. Holtz, one of the petitioners, temporarily resided in Washington, D. C., at which time he was specially appointed to handle the distribution of 16 mm. films in connection with the promotion and sale of war bonds for the Treasury Department.

2. The tax years in controversy are the calendar years 1949 and 1950. Petitioners executed joint income tax returns for these years, prepared on a cash basis, and duly filed same with the then Collector of Internal Revenue at Portland, Oregon. Photostat copies of these returns are attached hereto as Exhibits 1-A and 2-B. Petitioners claimed deduction of \$83,316.29 on their 1950 return as "bad debts arising from sales or services." This deduction was explained in Schedule C-2 of the return as "payments made to the U. S. National Bank as guarantor of business debts." Respondent determined that the amount of \$83,316.29 represented a

non-business bad debt, not a business bad debt as claimed by petitioners, and accordingly disallowed the deduction so claimed. Respondent treated this amount as a non-business bad debt under Section 23(k)(4) of the Internal Revenue Code of 1939.

3. The deduction of \$83,316.29 represented payments made in January and March of 1950 by the petitioners as guarantors to the U. S. National Bank of Portland, Oregon, on notes of Screen Adette Equipment Corporation. Attached hereto as Exhibits 3-C and 4-D are photostat copies of letters dated January 11, 1950 and March 8, 1950 from the U. S. National Bank of Portland, Oregon to the petitioner Merriman H. Holtz.

This corporation was organized in 1945 to engage in the sale and distribution of motion picture equipment and accessories, and has its offices in Seattle, Washington; Portland, Oregon; San Francisco and Los Angeles, California. Petitioners were the owners of 500 of the 503 shares of its stock outstanding. The petitioner Merriman H. Holtz was president, general manager, and actively engaged in its operation. In addition to the original capital invested by petitioners, sums were required in connection with its operation, normal growth and expansion. The corporation obtained these sums from the U. S. National Bank of Portland, Oregon. The loans were personally guaranteed by the petitioner Merriman H. Holtz who pledged as collateral certain listed common stocks then owned by the petitioners and having a then market value sub-

stantially in excess of the market value of the loans. Attached hereto as Exhibit 5-E are photostat copies of the bank's ledger pages showing the account of the corporation and its borrowings, all of which were guaranteed by the petitioner Merriman H. Holtz.

In October, 1949 the corporation filed a voluntary petition in bankruptcy in the U. S. District Court for the District of Oregon. Thereafter it never resumed business operations and was dissolved by proclamation of the Governor of the State of Oregon on December 29, 1950. In the bankruptcy proceeding the creditors received 0.038 per cent upon claims filed by them. In January and March of 1950 the U. S. National Bank of Portland, Oregon, sold the collateral securities pledged by the petitioners as guarantors for the indebtedness of the corporation. The bank realized \$83,-316.29 from the sale of the securities, which amount was applied toward the indebtedness of the corporation.

Sale of the securities by the bank was made at a time when the market was at its lowest due to the commencement of the Korean conflict. The proceeds from the sale of the securities were not sufficient to satisfy the loans in full and there remained owing by the petitioners upon their guaranty the amount of \$64,119.34. At the time the collateral was pledged with the bank, the market value of the securities was substantially in excess of the loans.

4. In 1932 petitioners organized Screen Adettes Inc., an Oregon corporation. In 1949 and 1950 they owned 91 of the 100 shares of capital stock outstanding. The corporation has been engaged in the distribution and sale of 16 mm. films from its inception. In 1949 and 1950 it sold audio visual equipment and accessories in addition to distributing 16 mm. films. Petitioners made advances from time to time to this corporation for working capital. In October, 1949 a loan of \$1,000.00 was made. This was repaid in monthly installments during the year 1951. In addition the corporation borrowed money from time to time from the U. S. National Bank of Portland, Oregon. These loans were personally guaranteed by the petitioner Merriman H. Holtz. Attached herewith as Exhibit 6-F are copies of the bank ledger pages showing the account of the corporation and its borrowings. The petitioner Merriman H. Holtz was president and managing officer of the corporation. He was actively engaged in its affairs.

5. During the years 1949 and 1950 the petitioner Merriman H. Holtz was president of Pictures Inc., an Oregon corporation. This company was organized in 1930 and remained inactive until 1949 when it began operations involving the sale and distribution of 16 mm. films in the Territory of Alaska. The company has been in operation from 1949 to date. The petitioner Merriman H. Holtz was the manager of the business and advanced funds to the corporation as required for its operation.

Petitioners owned 99 of the 100 outstanding shares of capital stock of the corporation in 1949 and 1950.

6. The petitioner Merriman H. Holtz was engaged in the sale and distribution of audio visual equipment and accessories as an individual proprietorship for part of the year 1950. He continued to operate this business in 1951 and subsequent years. The gross profit from this business in 1950 was \$2,066.05. In 1951 the gross profit from this business amounted to \$4,911.88 and the net income was \$2,450.76. In 1952 the sales and gross profit of this business were \$18,606.79 and \$4,479.20, respectively. It was necessary on occasion for petitioner Merriman H. Holtz to borrow sums from the U. S. National Bank of Portland, Oregon, in connection with the operation of this business, and on these occasions he would assign invoices representing sales of equipment to the bank as collateral.

7. In 1950 the petitioner Merriman H. Holtz was employed on a part-time basis at a fixed salary to sell 16 mm. films for Audio Film Center, an association that operated a film rental library in Portland, Oregon. This employment ceased in 1953. The petitioners had no proprietary interest in this association.

8. Petitioners were the owners of 90 per cent of the outstanding capital stock of Helene's Inc., an Oregon corporation, for many years prior to 1949 and 1950. This company has been engaged in the operation of a ladies' apparel retail store in

Portland, Oregon. This company borrowed various sums from the U. S. National Bank of Portland, Oregon over the years in connection with the operation of the business. The loans varied from approximately \$10,000.00 to \$25,000.00. The loans were guaranteed by the petitioner Merriman H. Holtz who pledged as collateral therefor certain listed common stocks owned by petitioners as well as life insurance policies carried on their life. Attached hereto as Exhibit 7-G are photostat copies of the bank's ledger pages showing the account of the corporation and its borrowings, all of which were guaranteed by the petitioners.

The corporation suffered substantial losses in its business after moving to a new location in 1947. In 1949 all of its assets were sold and the creditors were paid approximately 50 per cent in full settlement of their debts. In 1950 the final return of the corporation was filed for the fiscal year ending January 31, 1950. The petitioner Merriman H. Holtz was president and actively engaged in the business until operations terminated.

9. Attached hereto as Exhibit 8-H is a copy of the guaranty agreement executed by the petitioner, Merriman H. Holtz, and the U. S. National Bank of Portland, Oregon. Attached hereto as Exhibit 9-I is a collateral agreement executed by the petitioner, Merriman H. Holtz, and the U. S. National Bank of Portland. Attached hereto as Exhibit 10-J are the receipts for securities pledged by the petitioner, Merriman H. Holtz, to cover loans made by the bank

to the organizations described in the preceding paragraphs.

10. Attached hereto as Exhibits 11-K and 12-L are photostat copies of petitioners' income tax returns for 1951 and 1952.

11. The petitioner, Merriman H. Holtz, has been active since 1930 in the industry relating to the sale and distribution of 16 mm. films and audio visual equipment, supplies and accessories. He was one of the founders of the National Association of Visual Education Dealers, a national trade organization, which was formed in 1939 and is still in existence at the present time. He served as a member of the Board of Directors and as vice-president of the association from 1939 to 1948, and in 1948 and 1949 served as president thereof.

12. The attached exhibits shall be considered as having been offered and received in evidence in this proceeding.

/s/ MOE M. TONKON,
Counsel for Petitioners.

/s/ HERMAN T. REILING,
Acting Chief Counsel, Internal Revenue Service,
Counsel for Respondent.

Filed February 19, 1957, T.C.U.S.

The Tax Court of the United States
Washington

Docket No. 58455

MERRIMAN H. HOLTZ and HELENE TYROLL
HOLTZ,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

DECISION

Pursuant to the determination of the Court, as set forth in its Memorandum Opinion, filed June 26, 1957, it is

Ordered and Decided: That there are deficiencies in income tax for the taxable years 1949 and 1950 in the amounts of \$958.30 and \$671.66, respectively.

[Seal] /s/ G. G. WITHEY,
Judge.

Entered June 26, 1957.

Served June 27, 1957.

Entered June 27, 1957.

[Title of Tax Court and Cause.]

MEMORANDUM OPINION

Withey, Judge:

The respondent determined deficiencies in petitioners' income tax for the years and in the amounts as follows:

Year	Amount
1949	\$958.30
1950	671.66

The sole issue presented for our determination is the correctness of the respondent's action in determining that losses sustained by petitioners during 1950 as the result of discharging a guaranty on bank loans made to a corporation controlled by them are not deductible as business bad debts under section 23(k)(1) of the Internal Revenue Code of 1939, but are deductible only as nonbusiness bad debts pursuant to section 23(k)(4) of the 1939 code.

All of the facts have been stipulated and are found accordingly.

Petitioners, husband and wife, residing in Portland, Oregon, filed their joint income tax returns for 1949 and 1950 with the collector for the district of Oregon at Portland, Oregon. Inasmuch as the activities of Merriman H. Holtz are those with which we are here primarily concerned, "petitioner" or "Holtz" as hereinafter used has reference to him.

Petitioner has been engaged since 1930 in the business of selling and distributing 16 millimeter

film, audio visual equipment, supplies and accessories.

In 1930, petitioner organized Pictures, Inc., under the laws of the State of Oregon. Pictures, Inc., was inactive until 1949 when it began the sale and distribution of 16 millimeter films in the Territory of Alaska. The corporation has continued in operation since 1949. Holtz was the manager of Pictures, Inc., and advanced to it the funds required for its operation. During 1949 and 1950, petitioners owned 99 of the 100 outstanding shares of capital stock of the aforementioned corporation.

During 1932, petitioner organized Screen Adettes, Inc., pursuant to the laws of the State of Oregon. Since the time of its organization, Screen Adettes, Inc., has been engaged in the sale and distribution of 16 millimeter films in Oregon. During 1949 and 1950, petitioners owned 91 of the 100 shares of outstanding capital stock of Screen Adettes, Inc. Petitioner occasionally made advances to this corporation for working capital. In addition, Screen Adettes, Inc., on several occasions borrowed money from the United States National Bank of Portland, Oregon. All such loans were personally guaranteed by Holtz, who was president and managing officer of Screen Adettes, Inc., and was actively engaged in its affairs.

In 1945, petitioner organized Screen Adette Equipment Corporation under the laws of Oregon for the purpose of engaging in the sale and distribu-

tion of motion picture equipment and accessories on the Pacific coast. Petitioners were the owners of 500 of 503 shares of its outstanding stock. Holtz was president and general manager of the corporation and was actively engaged in conducting its operations. In addition to the original capital invested by petitioners, Screen Adette Equipment Corporation obtained working capital from the United States National Bank of Portland, Oregon. The amounts so obtained were in the form of loans which were personally guaranteed by Holtz who pledged as collateral certain shares of listed common stock owned by petitioners. At the time they were pledged by petitioner, the foregoing shares had a market value substantially in excess of the value of the loans.

In October, 1949, Screen Adette Equipment Corporation filed a voluntary petition in bankruptcy with the United States District Court for the District of Oregon. The corporation thereafter ceased its operations and was dissolved by proclamation of the Governor of the State of Oregon on December 29, 1950. Pursuant to the bankruptcy proceeding, creditors of Screen Adette Equipment Corporation received only 0.038 per cent upon the claims filed by them.

In January and March of 1950, the United States National Bank of Portland sold the collateral securities pledged by the petitioner as guarantor for the indebtedness of Screen Adette Equipment Corporation. The bank realized \$83,316.29 from the sale of the securities which was applied against the indebtedness of the corporation. Consequently, peti-

tioner was indebted to the bank in the amount of \$64,119.34 upon his guaranty.

Hotz was engaged as sole proprietor in the sale and distribution of audio visual equipment during part of 1950. In addition, during 1950, petitioner was employed on a part-time basis to sell 16 millimeter films for Audio Film Center, an association which operated a film rental library in Portland, Oregon.

Petitioners were the owners of 90 per cent of the outstanding capital stock of Helene's, Inc., for many years prior to 1949. Helene's, Inc., was a corporation engaged in the operation of a ladies retail apparel store in Portland, Oregon. Petitioner was president and was active in the management of Helene's, Inc. After moving to a new location in 1947, Helene's, Inc., experienced substantial losses and in 1949 all of its assets were sold. Creditors of Helene's, Inc., received approximately 50 per cent of their claims in full settlement.

During the years of its operation prior to 1949, Helene's, Inc., had borrowed various amounts from the United States National Bank of Portland for use as working capital. Such loans were guaranteed by Holtz who pledged as collateral certain listed common stocks and life insurance policies owned by petitioners.

Petitioners claimed a deduction in the amount of \$83,316.29 on their joint income tax return for 1950 as "Bad debts arising from sales or services." This deduction was explained in Schedule C-2 of peti-

tioners' 1950 return as "Payments made to U. S. National Bank as guarantor of business debt." The foregoing deduction represented payments made by petitioner in January and March of 1950 as guarantor on the notes of Screen Adette Equipment Corporation.

The respondent does not question the worthlessness of the indebtedness in issue or the year in which it is deducted as worthless, but has determined that petitioners are not entitled to the aforementioned bad debt deduction because the debt was not incurred in the conduct of petitioner's trade or business. The respondent therefore contends that petitioner's loss resulting from his guaranty on the notes of Screen Adette Equipment Corporation must be treated as a nonbusiness bad debt pursuant to the limitations of section 23(k)(4) of the 1939 Code.

The petitioners contend that Holtz was engaged in the business of promoting, organizing, financing and managing corporations during the years in issue and that the guaranty obligation on behalf of Screen Adette Equipment Corporation was incurred in the conduct of that business. They accordingly take the position that the loss in the amount of \$83,316.29 is deductible in full as a business bad debt under section 23(k)(1) of the 1939 Code.

The issue here presented depends for its resolution on the determination as to whether or not petitioner was engaged in a trade or business of his own during 1949 and 1950 to which the indebtedness in

question was proximately related. Robert Cluett, III, 8 T.C. 1178; Charles G. Berwind, 20 T.C. 808, *affd.* 211 F.2d 575; Jan G. Boissevain, 17 T.C. 325. If the indebtedness in question was not proximately related to petitioner's trade or business at the time it became worthless, it is deductible only as a non-business bad debt under section 23(k)(4) of the 1939 Code.

It is settled law that the business of a corporation is not the business of its officers. *Burnet v. Clark*, 287 U.S. 410; Jan G. Boissevain, *supra*.

However, a worthless debt, resulting from a loan by a stockholder to his corporation, may qualify as a business bad debt if the stockholder was engaged in promoting, organizing, financing and managing business enterprises. Henry E. Sage, 15 T.C. 299; Vincent C. Campbell, 11 T.C. 510; Langdon L. Skarda, 27 T.C. 137; *Giblin v. Commissioner*, 227 F.2d 692, reversing a Memorandum Opinion of this Court, decided October 29, 1954.

The authority of the foregoing line of decisions is applicable only in the exceptional situations in which the taxpayer's activities in promoting, managing and making loans or contributions to a variety of businesses may be regarded as so extensive as to constitute a business separate and distinct from the business carried on by the enterprises themselves. Charles G. Berwind, *supra*. In Vincent C. Campbell, *supra*, for example, in which we held that the taxpayers were in the business of organizing and operating corporations engaged in the retail coal

business, it was shown that from 1929 through 1944 the taxpayer had organized, managed and financed 12 corporations. In *Giblin v. Commissioner*, *supra*, the taxpayer, a practicing attorney on 11 or 12 occasions between 1926 and 1945, contributed his time and money to the development of various enterprises and business ventures. The United States Court of Appeals for the Fifth Circuit there held that the taxpayer was engaged in the business of promoting or dealing in business enterprises.

Petitioner has been engaged in the sale and distribution of motion picture films and equipment since 1930. During this period he carried on his activities through 4 separate business units: (1) Screen Adettes, Inc., a corporation engaged in the sale and distribution of 16 millimeter films in the State of Oregon; (2) Pictures, Inc., engaged in the sale and distribution of 16 millimeter films in the Territory of Alaska; (3) Screen Adette Equipment Corporation engaged in the sale and distribution of motion picture equipment and accessories; and (4) an individual proprietorship business conducted by petitioner for the purpose of selling audio visual equipment and accessories. In addition, the petitioners owned 90 per cent of the stock of Helene's, Inc., a ladies' retail apparel store.

Holtz frequently advanced funds to the aforementioned corporations, endorsed corporate notes or guaranteed bank loans to provide them with working capital, and was active in the management of their operations.

Early in 1950, the United States National Bank of Portland sold the securities pledged by petitioner as guarantor on loans made to the Screen Adette Equipment Corporation and realized \$83,316.29 from their sale. The proceeds were applied to the indebtedness of the corporation, resulting in losses to petitioner in the amount of \$83,316.29. Consequently, it is apparent that the losses in question were not incurred in or proximately related to the individual proprietorship business operated by petitioner during 1950. Moreover, insofar as we are able to determine from the record herein, the advances made by petitioner to the Screen Adette Equipment Corporation and the bank loans guaranteed by him were for the purpose of assisting that corporation in its business of selling motion picture equipment and accessories.

The history of petitioner's business in connection with the foregoing 3 corporations discloses no more than the customary activity of an individual who has devoted himself to carrying on a business enterprise by means of wholly-owned corporations. We do not think that the activities outlined herein are sufficiently extensive to establish the existence of a separate business of promoting, organizing, financing and managing businesses during 1950. Cf. *Dominick J. Salomone*, 27 T.C. 663; *Commissioner vs. Smith*, 203 F.2d 310, reversing 17 T.C. 135; *Hickerson vs. Commissioner*, 229 F.2d 631, affirming a Memorandum Opinion of this Court, decided December 29, 1954. Accordingly, on the evidence presented, we

are unable to find that the indebtedness in question bore a proximate relationship to the petitioner's trade or business either at the time the loan was made or at the time it became worthless. The losses in issue must therefore be treated as nonbusiness bad debts under section 23(k)(4) of the 1939 Code.

Decision will be entered for the respondent.

Served June 26, 1957.

Entered June 26, 1957.

In the United States Court of Appeals
for the Ninth Circuit

Tax Court Docket No. 58455

MERRIMAN H. HOLTZ and HELENE TYROLL
HOLTZ,

Petitioners,

vs.

COMMISSIONER OF INTERNAL REVENUE,

Respondent.

PETITION FOR REVIEW

Merriman H. Holtz and Helene Tyroll Holtz, Petitioners, by Moe M. Tonkon, Attorney, hereby file their petition for a review by the United States Court of Appeals, for the Ninth Circuit, of the decision of the Tax Court of the United States entered on June 26, 1957, (TC Memo 1957-106), determining a deficiency in Petitioners' 1949 and

1950 income taxes in the amounts of \$958.30 and \$671.66, respectively.

I.

Petitioners, husband and wife, filed their joint income returns for the years 1949 and 1950 with the Collector of Internal Revenue for the District of Oregon at Portland, Oregon, and at all times during said years and since, have been and now are residents of the City of Portland, Oregon.

II.

Nature of Controversy

The controversy involves the proper determination of Petitioners' income taxes for the years 1949 and 1950.

During the period 1930-1950, Petitioners organized, financed, operated and managed several corporations and a single proprietorship business. The principal activity of these enterprises consisted of the distribution, sale, and rental of motion picture equipment, accessories and film. In connection with the aforesaid financing activity, Petitioners advanced funds to these enterprises and on numerous occasions personally guaranteed their borrowings from banks.

In 1950, Petitioners paid to The United States National Bank of Portland (Oregon), the sum of \$83,316.29 as guarantors on notes of one of the corporations which they had organized, operated, financed and managed. This payment was treated as a business bad debt deduction on Petitioners' joint

income tax return for 1950. The Commissioner disallowed the deduction of this amount as a business bad debt fully deductible under Section 23(k)(1) of the Internal Revenue Code of 1939, and held that the payment represented a non-business bad debt, deductible as provided by Section 23(k)(4), hence to be treated as a short term capital loss, with resultant limited deductibility. The Tax Court of the United States sustained the Commissioner.

III.

The Petitioners being aggrieved by the findings of fact and conclusions of law contained in the findings and opinion of the Tax Court of the United States, and by its decision entered pursuant thereto, do hereby petition for a review thereof by the United States Court of Appeals for the Ninth Circuit.

/s/ MOE M. TONKON,
Attorney for Petitioners.

Duly verified.

Received and filed September 17, 1957, T.C.U.S.

[Title of Court of Appeals and Cause.]

NOTICE OF FILING PETITION FOR REVIEW

To: Commissioner of Internal Revenue, Internal
Revenue Service, Washington, D. C.

You are hereby notified that the Petitioners have filed with the Clerk of the Tax Court of the United

States at Washington, D. C., a Petition for Review of the decision of the Tax Court of the United States heretofore rendered in the above-entitled cause. A copy of the Petition for Review is hereto attached and served upon you.

There is also herewith enclosed:

(a) Designation of contents of Record on Review directed to the Clerk of the Tax Court of the United States.

(b) Statement of Points to be urged on appeal.

Dated at Portland, Oregon, this 16th day of September, 1957.

Respectfully,

/s/ MOE M. TONKON,
Attorney for Petitioners.

Service of copy acknowledged.

Received September 17, 1957.

Filed September 18, 1957, T.C.U.S.

[Title of Tax Court and Cause.]

STATEMENT OF POINTS

Come now the Petitioners above named, by their attorney, Moe M. Tonkon, and hereby assert the following errors which they intend to urge upon review of the United States Court of Appeals for the Ninth Circuit, of the decision of the Tax Court of

the United States on June 26, 1957, rendered in Docket No. 58455.

1. The Tax Court erred in holding that any deficiency exists with respect to Petitioners' income tax liability for the calendar years 1949 and 1950.

2. The Tax Court erred in holding that the activities of Petitioner, Merriman H. Holtz, during the period 1930-1950, inclusive, did not constitute the business of organizing, financing and managing businesses.

3. The Tax Court erred in holding that the activities of Petitioner, Merriman H. Holtz, during the period 1930-1950, were not sufficiently extensive to establish the existence of the business of organizing, financing and managing businesses.

4. The Tax Court erred in holding that the indebtedness in question did not bear a proximate relationship to Petitioners' trade or business either at the time the loan was made or at the time it became worthless.

5. The Tax Court erred in sustaining the Commissioner's disallowance of the business bad debt petitioners had deducted upon their 1950 income tax return under the provisions of Section 23(k)(1) of the Internal Revenue Code of 1939, in the sum of \$83,316.29, being payment made to The United States National Bank of Portland as guarantors on notes to one of the corporations which Petitioners had organized, operated, financed, and managed, and conversely the Tax Court erred in holding such

payment by Petitioners was a non-business bad debt deductible only as provided by Section 23(k)(4), Internal Revenue Code of 1939.

6. The Tax Court erred in that its opinion and decision are not supported by the facts and are contrary to law.

/s/ MOE M. TONKON,
Attorney for Petitioners.

Filed September 17, 1957, T.C.U.S.

[Title of Tax Court and Cause.]

CERTIFICATE

I, Howard P. Locke, Clerk of the Tax Court of the United States, do hereby certify that the foregoing documents, 1 to 10, inclusive, constitute and are all of the original papers on file in my office as called for by the "Designation of Contents of Record on Review," including exhibits 1-A thru 12-L, attached to the Stipulation of Facts, in the case before the Tax Court of the United States docketed at the above number and in which the petitioners in the Tax Court have filed a petition for review as above numbered and entitled, together with a true copy of the docket entries in said Tax Court case as the same appear in the official docket book in my office.

In testimony whereof, I hereunto set my hand and affix the seal of the Tax Court of the United

States, at Washington, in the District of Columbia,
this 26th day of September, 1957.

[Seal] /s/ HOWARD P. LOCKE,
Clerk, Tax Court of the
United States.

[Endorsed]: No. 15755. United States Court of
Appeals for the Ninth Circuit. Merriman H. Holtz
and Helene Tyroll Holtz, Petitioners, vs. Commis-
sioner of Internal Revenue, Respondent. Transcript
of the Record. Petition to Review a Decision of The
Tax Court of the United States.

Filed October 8, 1957.

Docketed: October 17, 1957.

/s/ PAUL P. O'BRIEN,
Clerk of the United States Court of Appeals for the
Ninth Circuit.